

South East Water's  
Response to  
Consultation on  
regulatory reporting

September 2016

## 1 INTRODUCTION

This document provides South East Water's response to the consultation on the review of regulatory reporting published in August 2016.

## 2 ANSWERS TO SPECIFIC CONSULTATION QUESTIONS

Below are responses to the specific questions raised.

Q1. What are your views on the content and format of the proposed tables in Appendix 1

We believe the evolution of the content and format of proposed tables is a sensible forward step. We understand that such revisions are required to ensure data is organised suitably for the pending PR19, however we also believe future requirements should be mindful of PR14 obligations and ensure the tables are compatible (and consistent) for monitoring against PR14 Final Determination outputs – we revisit this issue in question 3.

Q2. Do you have any comments on our proposal to elevate the reporting for water resources and bioresources from section 4 of the APR to section 2?

We believe the proposed changes are sensible.

Q3. Do the definitions for the water resources activities in RAG4 provide sufficient detail for you to complete pro forma tables 2A, 2B, 2D, 4D and 4E? (Note that the decision over the location of the boundary is outside the scope of this consultation as set out above).

We consider the definitions set out are broadly well defined.

We retain a number of comments carried over from our previous response and include:

*We believe companies should be able to vary from the guidance if there is suitable reason to do so – where this is the case companies should clearly state their reasons and altered approach in their methodology statement. We use debt management as a unique example to South East Water, where debt greater than 30 days old should be used as a driver. At South East Water we have been unable to use this as an appropriate driver since debt remains linked to the original customer type – hence unmeasured debt remains unmeasured debt (until written off or cleared). Issues have arisen as properties have become a measured property (particularly given our metering programme. Allocation using Ofwat guidance therefore inappropriately allocates associated cost to unmeasured customers that is no longer relevant. Ultimately this may therefore skew cost to serve values, which are based upon the current customer type base. We offer this example to support our view that prescribed guidance should be adaptable to unique circumstances.*

With regard to Debt management the allocation driver remain as per set out in June. However we believe the issue of debt will skew the cost to serve values, and this seems to have been

borne out in 2015-16 where a number of companies are indicating that unmeasured customers are more expensive to service than measured household customers. The result is that the measured premium potentially shows a false outcome, which is inconsistent with the Final Determination.

The latter point also brings forward a further issue that definitions should broadly be consistent with PR14 guidelines – since companies are monitored against their Final Determination outcomes. Altering the definitions can potentially make overall monitoring difficult. We appreciate the requirement to ensure definitions are in place for PR19, however we ask the question of how Ofwat, via changes in RAG guidance, will ensure backward monitoring remains consistent?

We also note that Ofwat have favoured to split out bulk supply costs to both resource and treated functions – regardless of whether water is delivered raw or treated. We have no overall issue with the requirement, however the requirement will be on the importer to provide such detail and in a robust manner.

As a final comment we would also seek clarification on meter reading on behalf of WaSCs. We currently consider this to be a non-appointed activity for both our sewerage providers. Our clarification is to determine whether this should be an appointed third party activity? For our Thames sewerage region we currently conduct all billing on their behalf, and hence we consider the whole activity to be non-appointed as part of the billing process (as per the income categorisation table in appendix 1, RAG 4.06). With our Southern sewerage provider we do not bill on their behalf, however we consider this still to be non-appointed. We consider this a suitable approach since the assumption is that our non-appointed cost would effectively register as appointed cost within our sewerage provider retail tables – thus we avoid double counting as an industry level. Given the guidance we consider this to be appropriate, however we feel clarification in the guidance would be useful to the industry to ensure a consistent approach is adopted.

Q4. Do the definitions for the bioresources activities in RAG4 provide sufficient detail for you to complete pro forma tables 2A, 2B, 2D, 4D and 4E? (Note that the decision over the location of the boundary is outside the scope of this consultation as set out above).

No comment of sewerage wholesale activities.

Q5. Please could you provide an estimate of the impact, for the changes that we have proposed to the boundary definitions for both water resources and bioresources at RAG4? (See questions 3 and 4 above). The impact should include an estimate of the change in Net MEAV resulting from the assets that have moved under the change in boundary definitions for both water resources and bioresources separately.

Given proposed changes to RAG guidance we do believe that three impounding reservoirs will switch over from their current MEAV position within the water resources function across to the network+ function. Associated direct operating expenditure is unlikely to be significantly affected, given most of the energy cost is present in the abstraction infrastructure leading to the raw water reservoir, i.e. cost will remain within the water resource function. However, the three impounding reservoirs are currently listed within the water resources function with regard to their MEAV. The estimated value of this switch from water resources to network+ is approximately £139m.

It should also be noted that MEAV is used as a cost allocation driver, and hence some further allocation of cost can be expected. Given local authority rates is currently £14.76m (2015-16), our accounting separation model indicates that the movement of these reservoirs would lead to a switch of operating expenditure from water resources to network+ would be approximately £650k.

There is also a consideration of related depreciation charge attributed to the above assets, with an estimated £40k (assuming no further significant investment) switching from water resources through to network+.

Q6. In the responses to our March consultation, some companies suggested that to avoid recognising numerous discrete connections as a raw water transport activity, a de minimis value (for example, length of pipe) should be added to the RAGs. This would clarify the allocation of raw water transport between water resources and water treatment. Under this approach if the length of pipe were below the threshold, the asset would be classified as water resources, and raw water transport if above. We propose an amendment to RAG4 to address this concern by making a specific reference to sites in the definition of raw water transport but have not added a de minimis value. Do you consider that a de minimis threshold should be introduced? If yes, what should value of that threshold be?

As per our last response we consider there should be a level of materiality attached to the raw water transport and storage business units. Following the definitions strictly we clearly have an element of a raw water network that links water resources to water treatment. However the majority of sites physically have a small footprint that encompass both abstraction (water resources) and water treatment. We currently assume a common sense approach and assume no raw water network when considering allocation of cost, since we do not believe these business units were created to capture this type of inter-site activity. We would therefore support clarification in the RAG guidance to include a de minimus value (e.g. length of main) regarding the raw water network link between water resources and water treatment, and would suggest 1km is an appropriate length.